Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

DA 92-841

In the Matter of	)	
	)	
1992 Annual Access Tariff Filings	)	CC Docket No. 92-141
	)	
National Exchange Carrier Association	)	Transmittal No. 495
	)	
Universal Service Fund and Lifeline Assistance Rates	)	

MEMORANDUM OPINION AND ORDER SUSPENDING RATES AND DESIGNATING ISSUES FOR INVESTIGATION

Adopted: June 22, 1992;   Released: June 22, 1992

By the Chief, Common Carrier Bureau:

I. EXECUTIVE SUMMARY

1. As required by Section 69.3 of the Commission's Rules, 47 C.F.R. § 69.3, the Local Exchange Carriers (LECs) and the National Exchange Carrier Association (NECA) filed annual access tariffs on April 2, 1992, to become effective July 1, 1992. This Order reviews the annual filings and directs these parties, where appropriate, to refile rates in accordance with this Order.[1] This is the second annual access filing following the implementation of the Commission's price cap rules, and as such, presents the first opportunity for carriers to propose sharing and low end adjustments to the price cap indexes.

2. Tier 1 LECs[2] and NECA filed total access reductions of $463 million for the year. These reductions break down as follows: subscriber line charges will be reduced by $25.2 million, carrier common line charges will decrease $237.4 million, traffic sensitive-switched charges are proposed to be reduced by $172.4 million, (local switching rates are being reduced 53.9 million, local transport rates are being reduced $222.6 million, and information rates are being reduced $3.7 million) and special access charges are proposed to be reduced by $28.4 million.

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[1]Appendix A contains a list of those parties filing pleadings in this proceeding and lists the full and abbreviated names of the parties that we use in the text of this Order.

[2]Tier 1 companies have annual revenues from regulated telecommunications operations of $100 million or more. Tier 2 companies are companies having annual revenues from regulated telecommunications operations of less than $100 million. Tier 1 companies account for over 95 percent of total interstate access revenue.

3. Adjustments made in this Order will cause carrier common line charges to decline an additional $30.9 million, traffic sensitive-switched rates to decline an additional $10.5 million, and special access rates possibly to rise by $9.4 million.[3] In addition to these adjustments, this Order also suspends the $81.7 million of below-band local transport rate reductions made by several GTOC companies.

II. PRICE CAP CARRIERS

A. Sharing and low end adjustments to the price cap

1) Method of Allocation

4. Under the sharing requirement, price cap LECs that through efficiencies have earned in excess of 12.25 percent are required to share some of their earnings with ratepayers in the following year through a downward adjustment to the price cap. The low end adjustment mechanism entitles carriers whose earnings drop below 10.25 percent to raise rates to the 10.25 percent level. Together, these adjustments operate as a "backstop" to ensure that the basic price cap adjustment formula produces a result fair to both ratepayers and carriers. Under Section 61.45(d)(4) of the Commission's rules, carriers must allocate sharing obligations and low end adjustments among baskets on a cost causative basis.

5. The price cap filings generally present two methods of allocating sharing or low end adjustments among price cap baskets. Most price cap LECs elected to allocate these adjustments using relative proportions of basket revenues to total revenues,[4] while a smaller group elected to allocate sharing obligations according to basket by basket earnings.[5] We believe that

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[3]For price cap carriers, these results are primarily due to reallocation of sharing amounts among the baskets, and the adjustments to the Reserve Deficiency Amortization (RDA) exogenous change. For the rate of return carriers, these results are due to changes in forecasted expense and demand.

[4]Because rates are set based on costs, revenues should equal costs. For this reason, basket revenue can be used as a proxy for basket costs. United allocated sharing to the Interexchange basket based on earnings in that basket, and allocated the remainder of any sharing amounts among the other three baskets on the basis of their relative revenues. GTOC and GSTC allocated sharing or low end adjustment amounts among all four baskets but used only carrier common line revenue in the common line basket for the purpose of computing relative revenues. Nevada Bell allocated its sharing amount by relative revenues among only the Common Line, Traffic Sensitive, and Special Access Baskets.

[5]These LECs allocated the sharing and low end adjustment amounts among baskets so that each basket would earn the same rate of return. Thus, the sharing or low end adjustment amount in each basket depend on the earnings level in that basket. SNET applied its low end adjustment only to Common Line,

allocating sharing and low end adjustment amounts on the basis of basket revenues most closely comports with the goals of the Commission's price cap plan to move away from cost allocation systems and instead focus on price.[6] We therefore require that LECs allocate their adjustments to all price cap baskets based on the proportion of total revenue in each basket to total interstate revenue.

6. A carrier's obligation to share revenues with its customers is calculated on the basis of its total interstate revenues.[7] Apportionment of that obligation among all price cap baskets by revenue is most consistent with this approach. The price cap plan, which is designed to give LECs strong incentives to increase productivity and efficiency, stresses LEC overall productivity, and the sharing mechanism is keyed to that unified approach.[8] Thus, it is more consistent to share the benefits of overall increased productivity across all baskets, than to apportion those benefits on the basis of relative basket earnings or to target those benefits to specific baskets. The Commission specifically declined to order sharing or low end adjustments on the basis of individual basket earnings because under this approach, the sharing obligation could have been triggered for a company that had high gains for a single basket but had not reached the overall productivity gains reflected in the offset factor.[9] As pointed out by Allnet, the Commission created the sharing mechanism as a backstop to the price cap plan as a whole, not as a safety net to individual basket earnings levels.[10]

7. Apportioning a LEC's sharing or low end adjustments on the basis of basket earnings would require the Commission to review and analyze a carrier's allocation of joint and common costs among the baskets. This consequence of using an earnings-based allocator is inapposite to the Commission's stated objective of de-emphasizing cost allocations in the ratemaking process when it adopted price cap regulation. This fundamental flaw in an earnings-based

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since that basket had the lowest rate of return. Ameritech and Bell Atlantic assigned their sharing amounts to the Special Access and Interexchange baskets, since only in those baskets was the rate of return above 12.25 percent.

[6]See Policy and Rules Concerning Rates for Dominant Carriers, Second Report and Order, 5 FCC Rcd 6786, 6791 (1990) (paras. 34-35); and Erratum, 5 FCC Rcd 7664, (1990) (LEC Price Cap Order); Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, Order on reconsideration, 6 FCC Rcd 2637, 2673 (para. 77) (1991) (LEC Price Cap Reconsideration Order). In addition to being the method favored by price cap LECs, it is also the method most favored by petitioners.

[7]See LEC Price Cap Order at 6805 (para. 151); LEC Price Cap Reconsideration Order at 2679 (para. 92, 94).

[8]LEC Price Cap Reconsideration Order at 2679 (para. 92).

[9]LEC Price Cap Order at 6805 (para. 151).

[10]Allnet Petition at 3.

approach has not been cured by the carriers' stated reasons for re-opening the cost allocation debate: (1) allocating an adjustment to the basket that triggered the adjustment is most consistent with direct assignment principles; (2) basket earnings is a better surrogate for productivity than revenue; and (3) a revenue-based allocation of a low end adjustment mechanism results in upward adjustments to the price cap in baskets that are already generating sufficient revenues.[11] As stated above, we cannot reconcile these arguments with the Commission's explicit decision not to adopt basket-by-basket sharing and low end adjustment devices. Indeed, shifting the focus to prices and away from complex and inherently arbitrary cost allocation systems is one of the principal benefits of a price cap system.[12]

8. We therefore direct Bell Atlantic, Ameritech, GTOC, GSTC, Nevada Bell, United, and SNET to revise their filings in accord with this decision. We estimate that this will increase the interexchange rates for the regions as a whole by $26.0 million and the special access rates by $9.4 million, while lowering common line rates by $26.6 million and traffic sensitive rates by $8.8 million as compared to the proposals set forth in these carriers' annual access filings.

2. Fourth Quarter Recognition of Costs

9. Various petitioners argue that the LECs made dramatic expense adjustments in the fourth quarter of 1991 that resulted in substantial changes in reported earnings.[13] These petitioners characterize the recognition of these costs as LEC attempts to manipulate sharing obligations or low end adjustments in the LEC's favor. MCI characterizes NYNEX's filing as the most extreme example of manipulation of expenses.[14]

10. In developing the low end adjustment mechanism, the Commission cited its interest in creating a "backstop" mechanism that would prevent price cap LECs from becoming subject to possibly confiscatory earnings over a long period of time due to miscalibration of the price cap index formulas.[15] Because the cap formula does not reflect costs within a carrier's control, the formula does not cause the cap to change in response to most cost changes. Thus, the formulas are said to create a "benchmark." To improve earnings, a carrier must reduce its costs, decreasing them relative to the benchmark. The low end adjustment mechanism recognizes the possibility that the benchmark may create

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[11]Ad Hoc Petition at 14-15, 18; Ameritech Reply at 5; SNET Reply at 2-4.

[12]See also AT&T Petition at 4 and n.**** (allocations based on current cost allocation methods would be misleading for price cap LECs).

[13]See MCI Petition at 11; Ad Hoc Petition at 3-4; AT&T Petition at 10-12.

[14]MCI Petition at 11-12 (challenging NYNEX's decision to include one-time workforce reduction expenses taken in the fourth quarter in its calculation of the lower formula adjustment).

[15]LEC Price Cap Reconsideration Order at 2676 (para. 86).

too difficult a challenge to LEC efficiency in some cases.

11. Petitioners now suggest that the Commission should look behind a carrier's reported total interstate earnings to decide whether a particular cost should be counted for the purpose of applying the low end adjustment mechanism or sharing. We find no support for making such a distinction in the LEC Price Cap Order or its reconsideration. To attempt to determine which costs are related to potential "gaming" of sharing or low end adjustments would lead us down a path of determining which business expenses are legitimate attempts to improve productivity and which are not. There is no suggestion in the Commission orders implementing price caps that this type of analysis is required. Even if the Orders permitted us to make such an analysis, petitioners have not suggested a means of distinguishing "legitimate" recognition of costs from "manipulative" ones.[16]

12. Furthermore, with respect to the earnings adjustments made in the fourth quarter, we have reviewed the specific adjustments for compliance with the Uniform System of Accounts (USOA) and generally accepted accounting principles, and find that this issue does not warrant investigation at this time.

13. Petitioners have also objected to NYNEX's decision to "normalize," or shift, these downsizing expenses into 1992 and 1993, the years in which these expenses will actually occur.[17] We find NYNEX's justification -- to avoid the significant increase in the price cap index for this year followed by a comparably significant decrease in the index next year -- to be persuasive. By shifting these expenses into 1992 and 1993, NYNEX forgoes a major increase in its price cap index which would enable it to significantly increase prices.

B. Effects of pricing flexibility

14. Various petitioners argue that, while LEC prices are below their price cap limits, the LECs have used the pricing flexibility available to them for potentially anticompetitive ends. They argue that LECs are anticipating switched access competition by lowering transport prices and raising rates for local switching, where future competition appears less likely to develop, within the traffic sensitive basket.[18] They assert that GTE, which filed significantly reduced below-band transport rates in several study areas,

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[16]For these same reasons, we find no merit in arguments that the low end adjustment mechanism can be used to defeat the carefully crafted policy of limiting the number of cost changes that are outside the carrier's control, e.g., exogenous costs, that can affect the price caps.

[17]MCI Petition at 7-8; AT&T Petition at 10.

[18]ALTS Petition at 12; MFS Petition at 3-7; Eastern Petition at 10-14 (also arguing that transport rates are coming down fastest for intermediate mileage bands where competition is greatest). The rates petitioned against, filed by Bell Atlantic, Pacific, BellSouth and SWB, are all within-cap, within-band rates.

should be subject to an investigation to ensure its rates are not predatory.[19] WilTel argues that SWB's 34 percent increase in its rates for dark fiber service, a service used by many competitors, violates the Communication Act's prohibitions on unreasonable and excessive charges.[20]

15. Parties seeking suspension of within-band, within-cap filings must meet the substantial showing set forth in Section 1.773(a)(1)(iv) of the Rules.[21] Section 1.773(a)(1)(iv) provides that such tariff filings will be considered prima facie lawful unless the petition either shows that the appropriate cost support information was not provided, or meets all four of the following tests: i) that there is a high probability the tariff would be found unlawful after investigation; ii) that the suspension would not substantially harm other interested parties; iii) that irreparable injury will result if the tariff filing is not suspended; and iv) that the suspension would not otherwise be contrary to the public interest. The general allegations raised by ALTS, MFS, WilTel, and Eastern concerning the rates proposed by Bell Atlantic, BellSouth, PacBell, and SWB, in no way overcome the prima facie presumption of lawfulness for below-cap within-band tariff changes. Thus they fail to provide sufficient reason to reject or investigate these rates.

16. GTOC's below band filing, on the other hand, raises different issues. The purpose of the lower pricing bands is to check predatory pricing. As the Commission has noted, the question whether prices are below average variable cost, is central to the determination of whether prices are predatory.[22] Thus, below band filings must be accompanied by a showing that the rates will cover average variable costs, and are otherwise just, reasonable, and nondiscriminatory.[23] GTOC is proposing to cut its rates substantially and in some cases to a level at or near the average variable cost reported in their study. GTOC's average variable cost showing, however, consists only of summary results of incremental cost studies. The full incremental cost studies supporting the summary results are required to evaluate the reasonableness of the filing, e.g., the type and cost of equipment used to provide transport and the amount of usage of the equipment. GTE has failed to adequately support its below-band rate filing. We therefore suspend GTE's below-band rates pending an investigation. GTE must provide the full incremental cost studies to support its filing and demonstrate that its rates are just, reasonable and

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[19]MFS Petition at 8-9; ALTS Petition at 3, 6, 18.

[20]WilTel Petition at 2-3 (arguing that since SWB is reducing its DS3 rates, dark fiber rates should also decrease).

[21]See LEC Price Cap Order at 6822 (para. 293).

[22]LEC Price CAp Order at 6824 (para.310).

[23]See LEC Price Cap Order at 6814, (para. 226) and 6824 (paras. 309-311); LEC Price Cap Reconsideration Order, at 2699 (para. 137).

nondiscriminatory.[24]

17. We therefore designate the following issues for resolution in this order:

(1) Are GTOC's below band rates above GTOC's average variable costs?

(2) Are GTOC's rates otherwise just, reasonable, and nondiscriminatory?

To better address these issues, we require GTOC to file a full incremental cost study supporting the summary results previously filed.

C. Tax Related Adjustments

1. Excess Deferred Tax Reserve

18. AT&T states that Ameritech filed an exogenous cost change (and an increase in its PCI) because of reductions in the amount of surplus deferred tax flowback (SDT)[25] available to it in the base year.[26] AT&T maintains that the Commission should review Ameritech's 1991-1992 excess deferred reserve amount, and suggests a disallowance of $3.6 million. AT&T asserts that Ameritech failed to provide any justification for the magnitude of the excess deferred tax reserve decrease, which gives rise to the excess deferred tax exogenous cost increase.[27]

19. Ameritech responds that the Excess Deferred Tax reserve exogenous change reflected in its 1991 annual access filing was too low. Ameritech states that it is correcting that error in the 1992 Access filing "for prospective

[24]Rates that cover average variable costs are not necessarily just, reasonable, and nondiscriminatory. Such rates are still subject to challenge under Section 204 of the Act, 47 U.S.C. § 204, and complaints may be filed under Section 208 of the Act, 47 U.S.C. § 208. LEC Price Cap Reconsideration Order at 2699 (para. 137).

[25]Prior to 1986, the LECs had a tax benefit resulting from their accrual of deferred taxes at a 46 percent rate, based largely upon the higher depreciation rates allowed for tax than for regulatory purposes. The Tax Reform Act of 1986 reduced the corporate tax rate from 46 to 34 percent, and thus the LEC deferrals at a 46 percent rate overstated the amount of tax that would ultimately have to be paid. Starting in 1987, when lower tax rates took effect, the LECs were able to realize the financial benefits of their over-deferrals, and the benefits continue over the useful life of the affected plant purchased prior to 1987. However, as that plant reaches the end of its useful life, the surplus tax deferrals are reduced.

[26]AT&T also notes that Rochester failed to reflect a reduction in New York State property tax. AT&T Petition, Appendix H at 1-2. Rochester conceded the point and filed Transmittal No. 167 on May 27, 1992 to reflect this exogenous cost change.

[27]AT&T Petition at 13-15.

application only." Ameritech asserts that this error caused understated rate base levels and exogenous cost changes resulting in erroneously low PCIs in the 1991 filing. Ameritech states that its 1992 PCIs reflect the accurate level of excess deferred taxes.[28]

20. Petitioners also challenged BellSouth's and United's surplus deferred tax flowback. Petitioners argue that on a percentage basis, BellSouth and United filed reductions in excess deferred taxes that were 157 percent and 129 percent higher, respectively, than the average of the other LECs.[29] Sprint also requests clarification of SWB's federal income tax rate for calculation of its deferred income tax balances.[30]

21. BellSouth states that it reduced its flowback of excess deferred taxes more than other price cap LECs because BellSouth has higher depreciation rates than the industry average, creating a faster flowback of the benefit of excess deferred taxes than the industry average. Another reason for the decrease in BellSouth's flowback of excess deferred taxes, BellSouth asserts, is completion of its inside wire amortization in 1992. BellSouth states that this results in a decrease in book depreciation in the July 1992 to June 1993 test period and thereby reduces the flowback of excess deferred taxes in this period as compared to prior periods.[31] United contends that decreases in its surplus deferred tax flow back are primarily the result of central office additions in the 1980's that were proportionally larger than historical activity. According to United, the turn around of excess deferred taxes occurs at different times for different companies based on the mix of capital additions in a given year, the depreciation rates, and timing of capital deployment.[32]

22. The LEC replies appear to address the excess deferred tax issues adequately. Petitioners have not shown that the LECs have failed to follow applicable accounting requirements. Accordingly, we conclude that this issue does not warrant investigation at this time.

2. Base Period Calculations

23. AT&T argues that several LECs, including US West, used an incorrect base period to calculate the exogenous cost changes for excess deferred income

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[28]Ameritech Reply at 11-14.

[29]AT&T Petition at 15-16.

[30]In reply, SWB states that, as it explained in a footnote included in Section 2.E of its D&J, the tax rate represents a weighted average of the various tax rates in effect in recent years, as they relate to SWB's deferred income tax balances. SWB Reply at 4-5.

[31]BellSouth Reply at 5-6 (also arguing that true-ups from prior period excess deferred taxes and other matters produced a one-time adjustment of $11 million).

[32]United Reply at 2-3.

taxes and the Investment Tax Credit (ITC). AT&T argues that US West used the calendar year 1991 as its base year, instead of the tariff year, as the rules require. AT&T contends that if US West had used the correct base period, its exogenous cost adjustment associated with SDT and ITC would have been lower.[33]

24. US West and the other LECs named by AT&T, all assert they used the correct base year. These carriers contend that AT&T may have been misinterpreting data filed pursuant to the Tariff Review Plan that required the price cap carriers to display 1991 base year information. In addition, SNET defends its use of October 1991 data to develop a base period for its exogenous cost change calculations, arguing that October most closely reflected the average monthly levels for 1991.[34]

25. Based on our review of the filing, cost support, and LEC replies, the LECs' use of base years does not raise an issue that warrants investigation at this time.

3. Amount for Taxes in Sharing Calculation

26. Sprint and Allnet argue that the amount for federal and state taxes included in some LECs' sharing calculation is vague or incorrect. Sprint contends that it could not confirm the correctness of Bell Atlantic's composite state and local income tax rate of 6.0 percent. Sprint also states that BellSouth and Ameritech, who have also included state tax factors in their sharing calculations, should clarify their calculations of composite state tax rates, including an identification of all state and local taxes included in these calculations.[35] Allnet states that Nevada Bell only accounted for Federal Tax in the gross-up calculation. Allnet argues that the <u>LEC Price Cap Reconsideration Order</u> affirmed that sharing should ". . . reflect relevant state, local and federal taxes . . . ."[36]

27. Ameritech replies that the individual tax rates were weighted together to calculate the composite rates based on each state's share of revenues, and that, therefore, Ameritech properly accounted for all appropriate state taxes in their gross up calculations.[37] Bell Atlantic asserts that it calculated the net return before income taxes by adding the state, local and federal income taxes to the interstate net return. Next, Bell Atlantic continues, it calculated the percentage of net return before income taxes figured in step 1, represented by its total state and local income taxes. According to Bell

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[33]AT&T Petition at 16-19 (also arguing that GTE, NYNEX, Rochester, and SNET may have made the same error).

[34]SNET Reply at 5. SNET argues that it restated its October data to reflect a blended year approach.

[35]Sprint Petition at 8.

[36]Allnet Petition at 4.

[37]Ameritech Reply at 8-9.

Atlantic, this percentage represents the weighted average composite state and local income taxes percentage for 1991.[38] BellSouth and NYNEX similarly defend their methodology.[39]

28. Based on our review of the filings, cost support, and LEC replies, the LECs' gross-ups of local, state and federal taxes do not raise issues which warrant investigation at this time.

D. Reserve Deficiency Amortization (RDA)

29. The LEC Price Cap Order required LECs subject to reserve deficiency amortizations (RDAs) at the time price cap regulation was implemented to treat the expiration of the RDAs as an exogenous cost adjustment.[40] In this manner, once carriers had been compensated for depreciation reserve deficiencies dating from the early 1980s, ratepayers would see a downward adjustment in rates reflecting the end of the amortization.[41] Based on our review of the filings, a number of carriers appear to have understated the exogenous cost decrease for RDA expiration.[42]

30. A review of last year's exogenous changes for US West shows that it did make RDA average net investment adjustments in excess of the required amounts by approximately $4.1 million, $2 million, and $0.9 million for, respectively, the Common Line, Traffic Sensitive and Special Access rate elements. We have taken these excess amounts into consideration in our examination of US West's average net investment adjustment and find that additional adjustment is still required this year.

31. Also, we find that GSTC, GTOC, Nevada Bell and SWB did not make adequate adjustments to their average net investment even after taking into account the partial year adjustment made in the 1991-92 annual filing.[43] In each case these companies made adjustments of about 21 percent of their amortization reduction adjustments. The reserve adjustment should be 50 percent of the RDA amount (displayed in chart EXG-1, Col (E), Line 100 i.e., the average of the amounts included in the rate base at the beginning of the period and at the end of the period).

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[38]Bell Atlantic Reply, Appendix A, Item 2 at 1.

[39]BellSouth Reply at 3-4; NYNEX Reply at 6 and Appendix G.

[40]An RDA is an addition to expenses which corrects for depreciation rates having been set too low in the past.

[41]LEC Price Cap Order at 6808 (para. 173).

[42]See also AT&T Petition at 19; MCI Petition at 12-13; Sprint Petition at 3-4; Ad Hoc Petition at 20.

[43]See GTE Reply at 9, SWB Reply at 3-4, US West Reply at 5-6 (arguing that the exogenous adjustment seems smaller this year because some of the adjustment happened at last year's annual access filing).

32. SWB, Nevada Bell and Pacific did not sufficiently respond to Sprint's claim that they should use the current Federal Income Tax rate of .34 to calculate the accumulated deferred income tax adjustment (EXG-1, Col. (E), Line 200) in making their exogenous changes for RDA.[44] We recognize that the deferred taxes were accrued at higher rates, but the difference between the higher accrual rates and the current rate of 34 percent can be included in the excess deferred tax reserve. There is a separate exogenous adjustment for excess deferred taxes, and we believe that in reducing their reserves SWB and Nevada Bell are double counting the effect of the excess deferred taxes.

33. We also examined petitioner's claims that NYNEX understated its RDA adjustment by failing to reflect the correct federal income tax rate in its calculations. NYNEX provides an adequate response to these claims. To the extent that, as we understand the NYNEX response, the rate differences result from associated adjustments which are not accounted for by other exogenous changes and are consistent with the methodology used to calculate the rates in effect, we accept NYNEX's RDA adjustments as filed.

34. The adjustments discussed in this subsection resulted in additional exogenous decreases for RDA[45] as follows:

	CL	TS	SA	IX
GSTC	$297,000			
GTOC	$ 14,148			
Nevada Bell	$ 11,364	$ 3,298	$ 756	
PacBell	$ 67,000	$ 35,000	$ 15,000	
SWB	$576,000	$302,000	$170,000	
US West	$108,000	$153,000	$ 26,000	
Total	$1,073,512	$493,298	$211,756	

These carriers shall reflect the additional exogenous change reductions in their price cap adjustment filings.

E. Inside Wire amortization

35. Various petitioners argue that different LECs have made errors in their calculation of the inside wire amortization. MCI argues that United understated its inside wire exogenous adjustment by $2.2 million.[46] For

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[44]Sprint Petition at 3-4; SWB reply at 3; Nevada Bell Reply at 6-8. PacBell did not respond to SWB's argument.

[45]Adjustments were calculated on the basis of the following: Depreciation Reserve (Line 190) equals 50 percent of Depreciation Expense (Line 100); Accumulated Deferred Income Tax (Line 200) equals 34 percent of Depreciation Reserve (Line 190); Net Return (Line 130) equals 11.25 percent of Net Rate Base (Line 210); and FIT (Line 140) equals .5151 percent of Net Return (Line 130).

[46]MCI Petition at 14.

example, Sprint asserts that if SWB and US West had used the proper federal income tax (FIT) factor, the exogenous cost change associated with inside wire FIT would be $363,182 and $183,640 -- $329,182 and $169,571 more than claimed -- respectively.[47] Sprint also alleges that the effect on BellSouth's total revenue of inside wire amortization may be understated because of BellSouth's assumed increase in its inside wire expense less depreciation of $104,660. Sprint states that this increase is counter-intuitive, given that inside wire expenses are being phased out of the rate base and that BellSouth's rate base and depreciation expense have, as expected, declined.[48]

36. In response, the carriers argue that their calculations are correct. BellSouth argues that Sprint's allegation that the revenue effect associated with BellSouth's inside wire amortization may be understated is flawed because Sprint focuses on post-separations results. BellSouth claims it is the interrelationship of separations allocators that causes the results pointed out by Sprint.[49] Similarly, United contends that its significant reduction in inside wire investment produces a cost shift among access elements due to the change in investment-based allocation, under Part 69. United states the Commission sanctioned this methodology last year in the context of the 1991 Annual Access Tariff filings.[50] SWB specifies a tax formula which it alleges verifies that SWB's FIT expense calculation is correct and that SWB used the appropriate FIT ratio.

37. Based on our review of the filing, cost support, and LEC replies, the LECs appear to address the inside wire amortization issue adequately. Accordingly, we conclude that this issue does not warrant investigation at this time.

F. <u>Allocation of Exogenous Costs Among Baskets</u>

38. Ad Hoc argues that various carriers did not allocate exogenous cost

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[47]Sprint Petition at 2.

[48]<u>Id</u>. at 3.

[49]BellSouth Reply at 7-8. Specifically, BellSouth maintains, in those states where the Basic Allocation Factor (BAF) was larger than the separations percentage of the big three investments (Central Office Equipment, Cable and Wire facilities and Information Origination and Termination) the completion of amortization of inside wire investment and removal of such investment caused the separations percentage of the big three investments to decrease and the resulting separations percentage of Network Operations Expense to decrease. <u>Id</u>. at 8. In those states where the BAF was less than the federal separations percentage of the big three investments, the removal of inside wire investment caused the separations percentage of the remaining big three investments to increase, which caused the separations percentage of Network Operations Expenses to increase. <u>Id</u>.

[50]United Reply at 4, <u>citing</u> Annual 1991 Access Tariff Filings, 6 FCC Rcd 3792, 3795 (para. 24) (Com.Car.Bur. 1991) (<u>1991 Annual Access Tariff Order</u>).

changes to the different service baskets on a cost causative basis. For example, Ad Hoc contends that Part 69 is an unreasonable basis for assigning exogenous cost changes associated with subscriber plant factor (SPF) and dial equipment minutes (DEM), as US West did.[51] Ad Hoc prefers an approach using direct assignment principles.

39. US West responds that no single allocation methodology works in all instances, and that Part 69 is a reasonable proxy for cost causation for allocating exogenous costs. Bell Atlantic maintains that it did, in fact, apportion inside wire related exogenous cost changes properly. Bell Atlantic states that the method it used -- allocating inside wire-related exogenous cost changes to the appropriate baskets on the basis of average net investment -- is the same methodology the Commission ordered Bell Atlantic to employ in the 1991 Annual Access Tariff Filings.[52] Rochester, Nevada Bell, SWB and NYNEX dismiss Ad Hoc's challenge to this method of assigning costs, asserting that (i) this method is consistent with cost-causative principles; and (ii) the Common Carrier Bureau specifically rejected this challenge last year -- Ad Hoc provided no basis for the Bureau to reach a different decision this year.[53]

40. The LEC replies appear to sufficiently address this allocation issue. Therefore, we conclude that this issue does not warrant investigation at this time.

G. Ameritech ONA rates

41. Pursuant to the price cap rules, Ameritech's introduction of Open Network Architecture (ONA) rates prior to January 1, 1992 requires Ameritech to incorporate those rates into its price cap indexes at the next annual filing.[54] Ad Hoc requests clarification that Ameritech's ONA rates remain subject to the ongoing investigation of ONA rates.[55] It is our general practice to investigate any subsequent change, however slight, of rates subject to an ongoing investigation. We therefore make the requested clarification in our ordering clauses.

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[51] Ad Hoc Petition at 17-19.

[52] Bell Atlantic Reply, Appendix A, Item 3, at 1 citing Annual 1991 Access Tariff Filings 6 FCC Rcd 3792 (Com.Car.Bur. 1991) (arguing that the Commission declined to require a single methodology for apportioning costs to the baskets).

[53] Id. at 4-5; SWB Reply at 2-3; NYNEX Reply, Appendix C at 4.

[54] As a result of Bureau Order, Ameritech's existing feature group rates will coexist with ONA rates through June 30, 1993. Amendment of Part 60 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture, CC Docket No. 89-79, 7 FCC Rcd 3003 (Com.Car.Bur. 1992). Ameritech Tr. 624, filed May 15, 1992, implements that decision.

[55] Ad Hoc Petition at 21. See Open Network Architecture Tariffs of Bell Operating Companies, CC Docket No. 92-91, 7 FCC Rcd 2604 (Com.Car.Bur 1992).

H. Miscellaneous Errors in Index Calculations

42. As in last year's filing, we developed a spreadsheet to verify the computation of the LECs' price cap indexes. As detailed in Appendix B, most LECs have computed their indexes correctly. However, four GTOC tariff entities (Illinois, Indiana, Idaho/Montana, and Oregon) have miscomputed their Interexchange PCIs and/or actual price indexes (APIs). In addition, NYNEX has miscomputed its Common Line PCI. These carriers are directed to revise their PCIs and APIs to reflect their correct levels in their price cap adjustment filings as indicated in Appendix B.

I. Allocation between Regulated and Non-Regulated Activities

43. MCI argues that the LECs have a significant incentive to understate the allocation of costs to nonregulated subsidiaries and that significant shifts in regulated versus nonregulated usage of facilities probably go unreported and undiscovered. MCI maintains that the Commission should conduct its own analysis of the LECs' Automated Reporting Management Information System (ARMIS) 495A and 495(B) reports,[56] and should calculate an appropriate exogenous cost adjustment to the LEC PCI on that basis.[57]

44. In response, Ameritech states that completion of these reports, which display any reallocation of shared investment from regulated to nonregulated, would readily show any improper investment shifting. Bell Atlantic maintains that there is no need for the Commission to analyze these reports, and adds that its method of separating costs between regulated and nonregulated activities is subject to an annual independent audit. Several carriers assert that they did not reallocate additional investment from regulated to nonregulated accounts.[58] NYNEX states that it did not show an exogenous cost change resulting from reallocation amounting to a $15,816 reduction, because this amount would not affect the level of the PCI values and would have no effect on rate levels.[59]

45. The LEC replies appear to address this question adequately. The petitioners have not shown that the LECs failed to consider the effect on PCI or revenues of changes in allocating investment and expense between regulated and non-regulated activities. From our analysis, we find that changes reflected in the ARMIS 495(A) and (B) reports would result in only de minimis adjustments. Further, audit efforts by Commission staff have been

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[56]This report displays the actual amounts of plant assigned to the regulated and non-regulated activities during the year. Form 495A displays a three year forecast of these amounts. See 47 C.F.R. § 43.21(e)(1) and (2).

[57]MCI Petition at 14-16.

[58]See Ameritech Reply at 11; Bell Atlantic Reply Item 5, at 1; SWB Reply at 7.

[59]NYNEX Reply, Appendix D at 2.

concentrating substantial efforts in examining the regulated/nonregulated allocation issue. We believe that these efforts are sufficient to uncover material failures to properly allocate investment and expenses between regulated and nonregulated operations. Accordingly, we conclude that this issue does not warrant investigation at this time.

J. SPF and DEM Adjustments

46. From our examination of the exogenous cost changes associated with the subscriber plant factor (SPF) and dial equipment minutes (DEM) transitions, it appears that carriers, with one exception, are making the required adjustments. NYNEX's DEM adjustment was below the expected level. In discussions with Bureau staff, NYNEX confirmed that an error in calculation resulted in an understatement of the DEM transition adjustment by $544,317. NYNEX is directed therefore, to make additional changes to its rates by increasing the common line and special access elements by, respectively, $55,590 and $24,306 and by reducing the traffic sensitive element by $624,213 in addition to the reduction already filed. NYNEX provided a satisfactory response to Ad Hoc's comments that it did not correctly calculate the common line federal income tax (FIT) expense associated with the DEM adjustment. Therefore, we do not require additional adjustments to correct this error.

K. Use of GNP-PI

47. The price cap rules require the LECs to use the Gross National Product Price Index (GNP-PI) to adjust their price cap indexes. At the time of the annual filing, the 45 day estimate was not available, and the LECs were granted a waiver allowing them to file using the Gross Domestic Product Price Index (GDP-PI).[60] The 1992 TRP Waiver Order also noted that LECs would be required to adjust their filings to reflect the GNP-PI when the 75 day estimate became available. Because that 75 day estimate is now available, the LECs are directed to revise their PCIs to reflect the 75 day estimate of the GNP-PI.

III. RATE OF RETURN CARRIERS

48. LECs under rate of return regulation have developed their rates using the same methods as in prior years. They have projected overall investment, expenses, and demand and then applied the separations methods and the Part 69 allocation methods in the Rules to develop individual rates. Rates are set so that the categories common line, traffic sensitive, special and interstate are targeted to earn an 11.25 percent rate of return.

49. As in previous years, we have conducted an independent statistical review of the projections of investment, expenses, and demand. This review is intended to provide a consistent, comprehensive, and reliable basis for evaluating LEC projections, and for identifying likely errors. If the statistical review indicates that projections are improbable and might produce

[60]See Commission Requirements for Cost Support Material to be filed with 1992 Annual Access Tariffs, 7 FCC Rcd 2153 (Com.Car.Bur. 1992) (1992 TRP Waiver Order).

excessive rates, we then examine the justification for those projections in the support material, petitions, and replies. If those projections still appear unjustified, we have computed adjustments. Our analysis is discussed in detail in Section III.A, infra. In Section III.B, infra, we discuss other rate development issues for individual LECs under rate of return regulation.

A. Bureau Analysis of Projections of LECs

1. Introduction: Tariff Review Plan (TRP) Analysis

50. We have reviewed LEC projections of costs prior to applying separations factors as well as their projections of minutes of use (MOU). Our review was based on the methods used in the 1991 Access Tariff Order.[61] Because only those LECs that have not elected price cap regulation are required to make these projections, our analysis of cost and demand trends was conducted for only six company study areas (COSAs).

51. Discussed below is our method of trend analysis of Telephone Plant in Service (TPIS) and Expense Less Depreciation (ELD). We also discuss our method of trend analysis of Carrier Common Line (CCL) MOU and Traffic Sensitive (TS) MOU. These are important categories of cost and demand in the TRP in terms of dollar value. The purpose of our trend analysis is to identify LEC forecasts of aggregate cost or demand that are substantially higher than the historical trend.

2. Report Card Tests

52. An important part of the trend analysis consists of report card tests. The report cards contain data reflecting the difference in forecasts in previous access tariff filings and actual data. Report cards measure the accuracy with which LECs forecasted cost and demand in previous annual access filings. In order to determine the accuracy of each LEC's forecasts, we rely on the three most recent test year forecasts from previous filings for which actual data are now available. The performance of each LEC, as indicated by its report card, is an important factor in the confidence we place in test year projections, as discussed in the 1988 Access Tariff Order.[62] Four separate report cards are used in reviewing cost and demand. The first is for TPIS and the second is for ELD. The third and fourth are for CCL MOU and TS MOU, respectively. The tests are constructed identically.

53. The report card data developed for the 1992 access tariff review are based on test year forecasts filed in the 1988, 1989, and 1990 annual access filings. Forecasts made by LECs for the 1988 test year are compared to actual results for the same year. Percentage differences between the forecasts and actual data are calculated. Forecasts and actuals for the 1989 and the 1990

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[61] 6 FCC Rcd 3792, 3802 (Com.Car.Bur 1991).

[62] Annual 1988 Access Tariff Filings, Memorandum Opinion and Order, 3 FCC Rcd 1281, 1285 (Com.Car.Bur.1987) (1988 Access Tariff Order).

test years are compared in the same manner.[63]

54. The 1992 report card data are a weighted average of the 1988, 1989, and 1990 percent differences. A weighted average is calculated separately for each report card. This weighting ensures that less emphasis is placed on the accuracy of earlier forecasts and more emphasis on the accuracy of more recent forecasts. Hence we assign lower numerical weights to earlier report cards than to later report cards. A weight of 1 is assigned to the 1988 results, a weight of 2 is assigned to the results for 1989, and a weight of 3 is assigned to the results for 1990.

55. The report card tests display the overall accuracy of the forecasts made by LECs during the last three test years. To the extent that LECs overforecast TPIS or ELD by more than 1 percent on average during the last three test years, the LECs receive a failing grade, for TPIS or ELD, respectively.[64] The results of the cost report card tests are displayed in Appendix C. To the extent that LECs underforecast CCL MOU or TS MOU by more than 5 percent on average during the last three test years, the LECs receive a failing grade in these categories. The results of the demand report card tests are displayed in Appendix D.

56. As in our previous access tariff Orders, LECs that fail for any category of report cards are subject to more stringent conditions, explained below, in determining whether and how much their forecasts should be adjusted. These evaluation procedures ensure that companies with good report cards have sufficient flexibility to forecast reasonable changes in aggregate cost or demand, and at the same time, guard against their departing unreasonably from historical experience. On the other hand, for companies that fail the report card test, less reliance is placed upon their forecasts that depart from historical experience.

3. Trend Analysis of Costs

57. The trend models for TPIS and ELD are constructed identically and include a constant term and a time trend variable. In the 1992 access tariff

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[63] In the 1991 access tariff review, we modified our method of reviewing the report cards from previous access reviews in order to incorporate a more recent test year. This required trending actuals in the first half of the 1990 test year forward, since actuals for the second half were not yet available. See 1991 Access Tariff Order, para. 88. We have decided to return to using the original method, because the benefit of using more current data did not outweigh the drawback of using estimated data.

[64] Last year we used a two percent boundary with our modified report card test to determine whether a LEC passed or failed the cost report card tests. Now that we have returned to the original test, we again use a one percent boundary, which was our original standard.

review, we conduct a Durbin-Watson Test for autocorrelation.[65] If the test concludes autocorrelation is present and a tentative forecast adjustment has been made, then the trend is run again with an autocorrelation adjustment, and the new trend becomes the basis for adjustment. The purpose of this modification is to avoid making unwarranted adjustments to the LEC's forecasts. The cost models, estimation method, and analysis results are described in Appendix C.

58. To derive tentative adjustments of TPIS and ELD, we use the same method in the 1992 access tariff review as in previous years. If the LEC forecasted growth is above an upper boundary for any category of cost, we decrease forecasted growth in that category to the upper boundary. The upper boundary is the LEC's historical mean growth rate plus one standard deviation if the LEC fails its report card. The upper boundary is the LEC's historical mean growth rate plus a 95 percent confidence interval (approximately two standard deviations), if the LEC passes its report card.

4. Trend Analysis of Demand

59. The trend models for CCL MOU and TS MOU are constructed identically and include a constant term and time trend. We modified our time trend from a one variable trend in previous reviews to a two variable trend in the 1992 access tariff review. The modification is made in order to account for what appears to be slower growth in demand. The additional variable is the square of the time which allows the trend to become non-linear. That in turn allows the model to capture slower growth. This modification is preferable to using time indicator variables, in part due to the difficulty of identifying the exact time period in which slower growth began. In addition to modifying our model, in the 1992 access tariff review, we conduct a Durbin-Watson Test for autocorrelation, as explained in III.A.3. If the test concludes autocorrelation is present and a tentative forecast adjustment has been made, then the trend is run again with an autocorrelation adjustment. The new trend then becomes the basis for making any demand adjustments. The purpose of this modification is to avoid making unwarranted adjustments to the LEC's forecasts. The demand models, estimation method, and analysis results are described in Appendix D.

60. To derive tentative adjustments of CCL MOU and TS MOU, we use the same method in the 1992 access tariff review as in previous years. If the LEC forecasted growth is below a lower boundary for any category of demand, we increase forecasted growth in that category to the lower boundary. The lower boundary is the LEC's historical mean growth rate minus one standard deviation if the LEC fails its report card. The lower boundary is the LEC's historical mean growth rate minus a 95 percent confidence interval (approximately two standard deviations), if the LEC passes its report card.

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[65] Autocorrelation in a time series creates a bias in statistical results. The Durbin-Watson test, employed by the Bureau for the first time in the current access filings, identifies autocorrelation.

5. Final Adjustments to Forecasts

61. The trend analysis identifies tentative adjustments to forecasts of cost and demand. The Description and Justification of the LEC's tariffs, petitions, replies to petitions, and other relevant cost support material are examined before any final adjustment is made. Examination of this material affirmed the tentative adjustment to the test year forecasts of ELD for Centel of Illinois and Lincoln Telephone Company, and the test year forecasts of CCL MOU for Centel of Florida, Centel of Illinois, Centel of Virginia, and Lincoln Telephone Company. No other adjustments were made based on our Bureau analysis of projections of LECs.

B. Other Rate Development Issues

1. NECA

a) NECA Pools

62. NECA filed rates amounting to a $104.9 million increase over its current rates at test year demand levels. Traffic sensitive rates are proposed to increase by $119.7 million or 17 percent. Rate decreases of $10.8 million or 8 percent are proposed for carrier common line rates. Special Access rates are being reduced by $4.0 million or 6 percent.

63. Various petitioners argue that NECA has understated demand and overstated costs for its pools. With respect to common line, AT&T contends that the amount attributed to the common line revenue requirement appears to be overstated by approximately $15.1 million due to an overstatement of costs. Sprint argues that revenue requirement increases for all of NECA's pools are inadequately justified and are unexpected, given that preliminary results for 1991 indicate earnings close to or above the authorized rate of return in each access category.[66] Sprint also claims that NECA failed to include the effects of demand stimulation created by the access cost decreases proposed by price cap LECs.

64. MCI asserts that the Commission should direct NECA to fully explain and justify the $21.6 million proposed increase in NECA revenue requirement that is due to the conversion of four of NECA's study areas from average schedule to cost settlement.[67] MCI also states that NECA proposes unusually large increases in the following expense categories without providing adequate cost support under Section 61.38 of the Commission's Rules: Plant Specific Expenses, Plant Non-Specific Expenses excluding Depreciation and Amortization, and Customer Operations and Corporate Operations. According to MCI, the increase in these areas will increase revenue requirement by $89.7 million. MCI wants justification for these expenses also.[68]

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[66]Sprint Petition at 8-9.

[67]MCI Petition at 30.

[68]Id. at 31.

65. In reply, NECA states that it does not anticipate significant demand stimulation from long distance price changes over the test period. In addition, NECA states that its cost projections are based on an "extensive analysis" of data provided by member companies, the expected impacts of changes in separations rules and other relevant factors.[69] NECA asserts that these projections are supported in NECA's filing, and reasonably reflect the costs expected to be incurred by NECA pool members as they continue to expand service in rural areas and upgrade their existing plant.[70] NECA further states that its cost projections are reasonable and consistent with historical trends. Id. at ii. Specifically, NECA states, cost company Common Line and Traffic Sensitive revenue requirements are projected to increase by approximately 10.3 percent on an annualized basis -- an increase slightly lower than the three year historical average growth level of 10.9 percent. Finally, NECA maintains that conversions of companies from average schedule to cost settlement shifted revenue requirement to cost settlements. NECA maintains the shift did not significantly effect total revenue requirement.

66. We have examined the issues raised in petitions regarding NECA's filing, as well as the filings and cost support. NECA's estimate of growth rates for demand and revenue requirement do not appear to be unreasonable, and we conclude that investigation does not appear to be warranted at this time.

b) NECA USF and LA Rates

67. The Universal Service Fund (USF) and Lifeline Assistance (LA) programs were established by the Commission to support, respectively, affordable telephone service among high cost LECs and low income subscribers. NECA files the USF rate based upon the average historical local loop costs of individual LECs and the LA rate based upon the costs of LA programs; the rates are assessed upon IXCs.[71] NECA now seeks to increase the USF rate from $0.3823 to $0.3901 per presubscribed line per month and to decrease the LA rate from $0.0789 to $0.0733 per presubscribed line per month. NECA states the changes reflect updates under Commission rules to USF cost data and NECA administrative expenses.[72]

68. MCI opposes the increase in the USF rate. MCI notes that the Commission recently approved a NECA filing which increased the USF rate, as of January 1, 1992, by 20 percent. MCI argues that high growth in loop costs and double counting of expenses are the source of the January 1, 1992 increases. MCI notes that despite only a 1.09 percent increase in access lines since that filing, NECA is proposing to raise rates by two percent. MCI believes that both

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[69] NECA Reply at 4, 18 (disputing AT&T's analysis on the basis that it assumes one-to-one correlation with access line growth).

[70] NECA Reply at i-ii.

[71] 47 C.F.R. Sections 69.603(c) and (d).

[72] 47 C.F.R. Section 36.631(e).

the existing and proposed USF rates are too high.

69. The Commission considered MCI's similar allegations about rates that are currently in effect during the last access review period and found the allegations without merit. We again find MCI's contentions unpersuasive in this review. We also find adjustments in NECA's current filing that result in a two percent increase are not unreasonable.[73]

2. Other Postretirement Employee Benefits (OPEB)

a) Petitions

70. MCI states that Centel, CBT, and NECA propose to increase their expenses for the test year to recover costs associated with a change in the accounting treatment of OPEB. Pursuant to instructions from the Financial Accounting Standards Board (FASB), companies following generally accepted accounting principles must reflect OPEB expenses on an accrual basis, rather than accounting for these costs on a pay-as-you go basis. MCI argues these costs should be disallowed for several reasons. MCI argues that rate of return carriers may have been compensated for these costs in the context of the Commission's 1991 represcription of the rate of return to 11.25 percent for interstate services. According to MCI, the costs and liabilities associated with OPEBs have been acknowledged by the investment market since the mid-1980's and as such have been reflected in the carriers' stock prices and costs of equity. MCI also contends that the rate of return may be too high for small to medium sized LECs, because it was set using Bell company share prices to determine the cost of equity. Thus, these small and medium-sized LECs are already enjoying some recovery of these expenses in their upwardly biased rate of return.[74] Carriers argue in response that their treatment of expenses associated with the implementation of SFAS-106 is consistent with the Commission's accounting rules and that these costs should be reflected in revenue requirements.[75]

71. The Bureau recently specified the accounting treatment for OPEB expenses that carriers subject to the Uniform System of Accounts must follow.[76] That Order provided that companies following generally accepted accounting principles must reflect OPEB expenses on an accrual, rather than a pay-as-you-go basis. Based upon our review of the petitions, filings, and cost support, the OPEB expenses claimed for the test year by rate of return carriers appear to be consistent with our accounting requirements and FASB requirements. We

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[73]We are however, concerned about the aggregate level of increase in the USF rate and anticipate examining this issue in a future proceeding.

[74]MCI Petition at 17-19.

[75]NECA Reply at 13-16; CBT Reply at 10-13; Centel Reply at 2-6.

[76]Open Network Architecture Tariffs of Bell Operating Companies, CC Docket No. 92-91, DA 92-483, released April 16, 1992.

conclude that this issue does not warrant investigation at this time.[77]

3. CBT

72. MCI argues that, in a number of cases, CBT has filed rates based on unexplained and unsupported cost increases. MCI characterizes as "speculative" a CBT proposal to increase its Power Expense by 16.1 percent over historical levels due to "anticipated rate increases" from its local utility.[78] MCI also objects to the proposed 11.92 percent increase in CBT's Sales Expense on the grounds that the increase was not sufficiently explained. MCI likewise objects to CBT's proposed increase in its Planning and Legal expenses by 59.11 and 50.40 percent, respectively, which, MCI asserts, CBT justifies based on state activities and regulatory reform.

73. MCI also argues that CBT has understated demand growth for traffic sensitive minutes, since CBT uses a higher demand growth figure for common line.

74. Finally, MCI argues that, for the third consecutive year, CBT alleged that it performed a new cost study which resulted in an increase in the interstate allocation for Central Office Equipment (COE)- Circuit Equipment and Cable and Wire Facilities (C&WF) categories. MCI contends that CBT's explanations for the increases are deficient.

75. CBT maintains that the increases in its expense and investment accounts are justified and will permit CBT to continue to operate efficiently and serve its customers.[79] CBT asserts that increases in investment accounts are the result of needs for new equipment. CBT also states that the Commission required change in the Subscriber Plant Factor (SPF) allocator is the main reason for a higher allocation to the interstate jurisdiction. Cincinnati maintains that without the change in SPF the interstate allocation for COE-Circuit Equipment and Cable and Wire Facilities would have decreased.

76. Additionally, with regard to MCI's allegations that there are inconsistencies in CBT's forecasted minutes of use (MOU), CBT suggests that the Carrier Common Line MOU projections be adjusted with reference to the Switched MOU data. Id. at ii.

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[77]Several price cap carriers seeking rate recognition of OPEB costs filed tariffs prior to the annual tariff review period. Those filings have been suspended for five months and are subject to investigation. Open Network Architecture Tariffs of Bell Operating Companies, 7 FCC Rcd 2604 (Com.Car.Bur 1992).

[78]MCI Petition at 21-25 (citing Annual 1990 Access Tariff Filings, 5 FCC Rcd 4177 (Com.Car.Bur. 1990) that rejected a depreciation increase as speculative).

[79]CBT Reply at i, 16.

77. We have reviewed CBT's cost support, including a statistical evaluation of CBT's cost and demand forecasts described above, and conclude that CBT's rates do not require investigation at this time. We therefore deny MCI's petition.

4. Equivalent LS1 and LS2 Rates

78. MCI contends that in violation of Section 69.205(d) of the Commissions Rules, CBT has proposed identical rates for its LS1 and LS2 Local Switching rate elements. MCI maintains that while both are priced at $0.0072, LS1 rates should equal 99.5 percent of LS2 rates.[80] CBT states that it is in compliance with the Rules regarding this issue, and describes its method of calculating LS1 and LS2 rates, and explains that identical rates result from rounding.[81] We have reviewed CBT's cost support and conclude that CBT's rates do not require investigation at this time. We therefore deny MCI's petition.

5. Centel

79. MCI objects to several of Centel's regulated expense and investment increases on the grounds that they are vague, inconsistent, or unjustified. MCI requests that the Commission hold Centel to the same inflation rate used by CBT. MCI also objects to the increases in Call Completion and Number Services expenses in Nevada on the basis of increased calling volume experienced by Centel-Nevada, arguing that the cost increases seem much larger than the volume increases.[82] MCI also questions Centel's General and Administrative expense increases and its Florida Marketing expenses. MCI Petition at 28.

80. Centel maintains that its access rates are fully justified and reasonable. Centel also objects to using an inflation rate borrowed from CBT because it is not based on Centel's expenses and thus has no relevance to Centel.[83]

81. The issues raised by MCI overlap our statistical evaluation described in Section III. These issues are addressed within that analysis.

6. General and Administrative Expense

82. AT&T contends that several companies have incorrectly made a direct assignment of a portion of General and Administrative Expense (Account 6720) to the interstate jurisdiction. AT&T maintains that all such expense should be assigned only after being allocated between state and interstate according to

[80] MCI Petition at 25.

[81] CBT Reply at 2.

[82] MCI Petition at 27-29.

[83] Centel Reply at iv-v.

the method described in Part 36.392 of the Rules.[84] The LECs identified by AT&T do not dispute that some General and Administrative costs have been directly assigned to the interstate jurisdiction, particularly those costs relating to the preparation of interstate tariffs.[85] These carriers maintain that the Commission has previously declared that expenses incurred for interstate tariff preparation should be recovered entirely from interstate rates, and add that these expenses are, in any event, de minimis.

83. We find that the companies have failed to justify direct assignment of Corporate Operations Expense to the interstate jurisdiction. Section 36.392(c) of the Commissions's Rules specifies that this expense is to be separated based on an allocation factor and not directly assigned. Chillicothe, Citizens Utilities of CA, Roseville, C-R, Kerman, Moultrie, and West River have failed to justify departure from the prescribed separations procedure. We find therefore that the assignments of general and administrative expenses to the interstate jurisdiction have been overstated for these carriers as follows:

Chillicothe	$198,671
Citizens Utilities of CA	$ 15,839
Roseville	$ 68,179
C-R	$ 5,362
Kerman	$ 4,851
Moultrie	$ 15,441
West River	$ 1,217

These carriers shall make appropriate adjustments to their tariff filings for the overstated assignments to the interstate jurisdiction. This finding is consistent with a similar finding in the 1990 Access Tariff Order.[86] NECA shall also adjust its rates to the extent that these adjustments affect its pool rates.

IV. IMPLEMENTATION OF PCI AND RATE ADJUSTMENTS

84. As the detailed discussion of these issues indicates, we have concluded that in some instances price cap LECs have improperly calculated their PCIs and other price cap rate limits, or have not adequately justified

[84]The companies identified by AT&T include Chillicothe, Citizens (California), C-R Telephone Company (C-R), Kerman Telephone Company (Kerman), Moultrie Independent Telephone Company (Moultrie), RTC, and West River Mutual Aid Telephone Corporation (West River). C-R, Kerman, Moultrie, and West River are issuing carriers in the GVNW Inc./Management (GVNW) FCC Tariff No. 1. AT&T Petition at App. K.

[85]Chillicothe Reply at 2-3 (costs of interstate tariff, Form 492 directly assigned); Citizens Reply at 1 (consulting fees, filing fees related to interstate tariff are directly assigned); Roseville Reply at 2-4; GVNW Reply at 3-4.

[86]Annual 1990 Access Tariff Filings, CC Docket No. 90-320 5 FCC Rcd 4177 (Com.Car.Bur. 1990) (para. 129).

those calculations. Rate of return LECs have in some cases committed apparent errors in their rate calculations, or have not adequately justified apparently anomalous and excessive projections of costs. If uncorrected, these filings would apparently establish excessively high access rates, despite the fact that the filings overall represent rate reductions. These excessive rates would be passed on to telephone subscribers in the form of unnecessarily high long distance or private line rates.

85. The Communications Act establishes alternative mechanisms to address these circumstances in Section 204(a) and Section 204(b), 47 U.S.C. §§ 204(a), 204(b). For these filings, Section 204(b) provides the more appropriate remedy. We currently conclude that under Section 204(b), the Commission may, inter alia, allow part of a change to go into effect based upon a written showing by the carrier and an opportunity for written comment thereon that such partial authorization is just, fair, and reasonable.[87] The tariff filing and review process has, procedurally, provided LECs and the public with the opportunity to submit these written comments and showings. Substantively, we believe it is preferable to calculate adjustments to correct apparent errors or failures of justification and allow the remainder of the rates to take effect without further delay, and that this action will be just, fair, and reasonable to LECs, access customers, and the public.

86. For price cap LECS, the adjustments are applied to correct the calculated PCIs. In most cases, where APIs are set close to or at the level of the PCI, the effect would be APIs that exceed the PCIs unless rates are adjusted downward. None of the price cap LECs have filed the additional support information and justification that would be required to justify above-cap rates because none of the LECs intended its rates to move above the cap. Refiling of PCIs to implement the necessary PCI adjustments, and refiling of APIs and rates that conform to the price cap limits, will ensure that LECs are in compliance with the price cap rules.

87. For rate of return LECs, as in prior years, we have computed adjustments to the proposed rates. These companies are directed to recalculate their filed rates so that the recalculated rates result in cost adjustments equal to those identified in this Order. The recalculated rates must be accompanied by a clear, reasonable explanation of how each adjustment was calculated.

88. NECA is directed to recalculate its CCL rates and individual LEC obligations for long term support payments in accord with the adjustments in this Order. Individual LECs are similarly directed to reflect these changes, as appropriate, in their CCL rates.

89. As in prior years, we wish to emphasize the limited nature and effect

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[87]Applications for review of the Commission's 1990 Annual Access Tariff Order and the Annual 1989 Access Tariff Filing, 4 FCC Rcd 3638 (Com.Car.Bur. 1989) challenging the Commission's authority to issue partial disallowances under Section 204(b) of the Rules, 47 C.F.R. § 204(b) are currently pending before the Bureau.